THE PUBLIC INSURABLE INTEREST

The possession of property exposed to destruction by the elements necessarily places the owners thereof in a position of holding a wager with fate. The ruin of men in the early days of commerce through the loss of such wagers as an outcome of disasters, as by fire or shipwrecks, led to the practice of lessening the risk of fate to the individual property-owner, through his entering into a counter wager or hedge with his fellow-men by a payment in advance to induce someone else to share in the risk. The practice of insurance became thus established without any specific provision of law. Later, such wager contracts were also to some extent entered into by parties having no property exposed to the elements. Later yet, or so soon as jurisprudence became shaped by a perception of the immorality of needless gambling, the courts of all nations recognized the necessity of establishing a distinction[1] between the legitimate risks covered by insurance and the illegitimate risks of gambling, and adopted a broad rule that insurance can be legally issued solely to those who may have an ownership or direct interest in a property exposed to risk of the elements or fate, or, as it is termed, an "insurable interest." Insurance contracts under this rule are permitted in almost any form the property-owner may desire. The term "insurable interest" has been broadly interpreted by the courts to apply to the owner of every sort of right in the business—creditor, trustee, consignor, consignee, indorser, lessor and lessee, mortgagor and mortgagee, purchaser, stockholder, and various other interests. The courts further recognize contingent interests as against loss of rents or of trade following a disaster, or legal liability, as for fire extending to neighbors as in France. Such peril may become greater than the

[1] "It is, therefore, essentially different from ordinary commercial transactions, and, as we have seen, according to the sense of the world from the earliest times, certainly the sense of the modern world, is of the greatest public concern."—*German Alliance Insurance Co.*, v. *Kansas*, 233 U. S. 389.

value of the property owned and is recognized as an "insurable interest" in all courts.

That the insurance contract is none the less in the nature of a wager contract has always been recognized, as by Anson,[1] Marshall,[2] Hadley,[3] and in recent legislative reports,[4] but the absolute necessity for insurance as a matter of public policy is also held to be a moral justification for a ratification of the form of wager; and surely it is better that a man should safeguard with his fellows rather than be compelled to wager risk of ruin at the hands of fate. The public policy of the world respecting insurance rests simply and solely on the doctrine of the equity of the "insurable interest."

Observe, however, that the "insurable interest" is a private interest as owner, creditor, trustee, or other direct interest in property, and always for private, not public, account. This fact alone is a fair reason for skepticism as to the merits of the "insurable interest" as a basis for court practice, on the broad ground that a public policy cannot rightly be based *per se* on any form of individual interest and cannot be righteous unless it can be shown that in practice such individual interest shall fully coincide or square with an inherent public interest. The writer believes in fact that "insurable interest" on the part of an insured person is not an adequate basis for any public policy, that it is immoral as gauged by the results of its universal use as such, that it is not a fact pertinent

[1] "A man who bets against his horse winning the Derby is precisely in the same position as a man who bets against the safety of his own cargo."

"The law forbids A to make such a contract unless he has what is called 'an insurable interest' in the cargo, and contracts in breach of this rule have been called mere wagers. But such a distinction is misleading. It is not that one is and the other is not a wager; a bet is not the less a bet because it is a hedging bet; it is the fact that one wager contract is and the other is not permitted by law which makes the distinction between the two. Apart from this there is no real difference in the nature of the contracts." Anson on Contracts, (2d American ed. of 4th English ed. Knowlton), p. 226 (Star, p. 174).

[2] "And yet, after all, it must be owned that the law descends greatly from its dignity when it lends its aid to any wager, however innocent."—Marshall, 1802 American ed., 1810.

[3] "In this case also the contract is a wager."—Hadley on insurance, *Economics*, p. 99.

[4] The New York Joint Legislative Committee's general report of 1911 on insurance makes repeated reference to gambling.

to wholesome law, and that on the contrary the insurable interest of the individual can be safely ignored provided he is limited to insurance so worded as to comply with the "public insurable interest."

This is not to say that a definable and luminous "public insurable interest" can be shown for all forms of insurance, nor that one such concept could rule all forms of property insurance alike. The case of fire insurance, as directly affecting the greatest number of people, is of primary interest, and is the main illustration hereinafter.

Attention is called to the circumstances attending fire loss, with its attendant costs, in the United States. The gross importance of this waste in the United States is, as the public more or less definitely knows, enormous,[1] and it is increasing, as the public may not so definitely know, with a rapidity that is relatively greater than our increase in wealth or in population.

By far the best basis for comparison with other countries is to take the "frequency of fire per capita." Statistics as to loss per capita, or fire waste as related to public wealth, or losses as compared to premiums, while much used in print, upon analysis are found to lack meaning until separated into "cost per fire" and "frequency of fire per capita," and then clearly will be found to rest on "frequency of fire per capita."

How tremendously the fire-waste[2] problem is growing with us is indicated by the figures given in Table I, which show the rate at which the number of fires per capita has been increasing in the great cities of the United States during the last few decades. The figures have been sorted out directly from the original fire records and include only fires with measurable loss that are properly classed as city fires, thus disregarding false alarms, chimney-soot blazes, vacant-lot bonfires, and suburban runs.

[1] "The United States destroys or permits to be destroyed by fire more property than any civilized country, and our national fire losses in proportion to our insurable values, are from six to twenty times those of any European nation."—Illinois Joint Legislative Report, p. 904, 1911.

[2] "The fire loss is an economic waste. Insurance repays nothing. It merely distributes the loss. Furthermore, there is nearly always a loss of property and an interruption to business, and possible loss of life, which is not compensated by the insurance,"—Commissioner Ekern, Wisconsin, 1914.

These digested figures of record emphasize the modern growth of a moral disease in America, particularly in the large cities where the increase of frequency of fire per capita since 1880 has been more than threefold. Similar averages for 1909–1910–1911 are for Paris, 7.9, for Marseilles, 5.9, for Liverpool, 8.7 and for Manchester, 6.9. For 1909–1910–1911–1912, in London, the average was 7.9. The average of the English and French cities was 7.46, or between one-fourth and one-fifth the American frequency per capita. The United States Consular Report of January, 1912, shows that Tokyo, Japan, had 2,717 fires in five years—a highly inflammable city as large as Chicago with about one-tenth the fires per capita.

TABLE I

THREE-YEAR AVERAGE NUMBER OF FIRES PER 10,000 POPULATION IN SIX LEADING CITIES OF THE UNITED STATES BY DECADES

	1879–81	1889–91	1899–1901	1909–11
New York (Manhattan-Bronx)	12.3	21.8	25.8	35.1
Chicago	15.0	27.0	34.7	38.4
Philadelphia	9.3	11.3	22.0	24.4
St. Louis	10.5	20.5	29.2	46.0
Boston	13.1	16.0	29.6	42.4
Baltimore	9.9	13.9	23.0	26.6
Average of the six cities	11.6	18.4	27.4	35.5

Space forbids refutation of apologists who attempt to smooth over the facts that fires in American cities and in the United States generally have increased so enormously per capita in one generation, and who say that a high frequency must be expected on account of our many wooden houses filled with modern devices, etc. As a matter of fact the United States has certain thrifty racial or religious communities where the inhabitants live and work in easily burnable buildings with inflammable contents and yet have as few fires per capita as do the Swiss[1] or the Japanese.

Too much emphasis cannot be laid on the fact that "frequency of fire per capita" is the prime cause of fire waste in any land. If

[1] "Switzerland is a country of wooden houses, yet the per capita fire loss there last year was only 2 per cent of the American per capita loss."—American Society Mechanical Engineers, 1913, Emerson.

the United States could reduce its "frequency of fire per capita" half-way toward that of today in England or France, or get it back to where it was but a generation ago, the entire appropriation for the navy could be far more than doubled without adding to the public burden. The grounds for such a statement are a matter of public record.[1] Our records are not appreciated because the public habit is to think only of the property burned, whereas this loss is but one item of expense in a great five-item aggregate, the other factors being the insurance cost, the fire department cost, the private protection cost, and the administrative cost. It is impossible to compute this great sum definitely, yet the joint legislative commissions of New York and of Wisconsin have estimated our annual loss at "upward of three-quarters of a billion dollars," an amount greater than the ordinary value of our wheat crop. This huge economic drain[2] is shown by the New York commission and other public reports to be less than one-half, possibly but one-third, accountable for by the property destroyed by fire, because of our utterly disproportionate costs for protection, distribution, and administration, all of which are a direct consequence of the frequency of fire per capita.

There can, however, be no hope of improvement in this direction so long as we do business under a system which is in direct violation of the legal principle that all contracts by which a principal wholly relieves himself from penalty incurred through neglect, by himself or by his servants, are unsound as creative of or maintaining public detriment.

Foreign countries gain their comparative immunity from fires, partly through an autocratic and military system which would not be tolerated here and which is beginning to break down in Europe and somewhat in the Orient. The legal defect exists in all countries, punitive laws do not correct it, and the bad effects merely show

[1] Department of the Interior, United States Geological Survey, *Bulletin 418*, "The Fire Tax and Waste of Structural Materials in the United States," by Wilson and Cochrane, 1910.

[2] "It is impossible to spend directly and indirectly on the luxury of fires each year the amount of $750,000,000 and not have to give up other luxuries; it is impossible to employ 500,000 men, in building, in insurance, in fire departments, who might otherwise be creating wealth, and not feel the strain of their support."—New York Legislative Report, 1911.

earlier and on a larger scale in North America. The average person in the United States has no conception of the social significance of fire waste; he pays the heaviest insurance prices in the world and the heaviest fire department taxes in the world, and he thinks that there his responsibility ends.[1]

Our state insurance commissioners strive in vain to instruct our public as to personal responsibility in repeated reports. The National Convention of State Fire Commissioners in 1911 resolved, "The chief factor for this situation is general carelessness and the utter lack of personal responsibility for the removal of causes productive of fires." These same students and public servants in state reports year after year point out that frequent fires increase the risk of city conflagration,[2] that adding fire department force merely adds to the gross cost,[3] that police measures do the same, that insurance does the same, that the effect of imposing fines or charges for fires simply adds to the things insured against, with insurance costs added. And no one can say that the public lacks such information in view of its constant publication and ease of access.

These pages are for those men who believe that every conceivable private action involves some question of public policy and that the sole opening into a better autonomy from out the confusion of modern conditions is to learn what constitutes appropriate public policy and to follow that path.

It is submitted that we must eventually meet the fire-waste problem by the method of direct attack[4] and that such a method does exist and that a definable and workable "public insurable interest" also exists.

[1] "So long as our citizenship views with complacency the destruction of insured property and feels horror only when the property destroyed is uninsured, we cannot expect any improvement or any lessening of the fire waste."—Commissioner Done, Utah, 1912.

[2] "The great massed insurable values of this country exist in our towns and cities, where they are liable to be swept away by conflagrations which vitally affect every member of the local community; in a lesser degree every citizen of the state; and in city conflagrations, every American citizen."—Illinois Commission Report, 1911.

[3] "As we permit fire to destroy such an immense amount of property we are necessarily under a high expense to put out these fires and prevent conflagrations."—Commissioner Hartigan, Minnesota, 1910.

[4] "We are waiting for the time when we shall be intelligent and far-sighted enough to attack this problem directly."—New York Legislative Commission, 1911, p. 50.

Every citizen has an insurable interest in every piece of burnable property in the country, regardless of actual legal ownership. This is true because every fire and every fire risk adds its quota, however small, to the maintenance of high insurance rates, high fire department charges, and heavy administrative expenses.[1] These fixed charges are borne by the whole community. Beyond this, however, betterment of fire insurance is vitally concerned with the stability of industrial society. How far-reaching this relation is may not be generally realized.[2] Insurance furnishes a large part of the confidence so essential to the conduct of the great credit business of every modern nation, its utility is greatest in sustaining the ninety-nine who do not have a fire, as well as great in saving from ruin the one who has a disastrous fire. Without it men would become unnerved and would shrink from assuming the responsibilities of business. We are all, then, partners, because we as a community cannot forego initiative and enterprise in one another.

The public insurable interest in any burnable property is greatest in the event of total loss, for a total loss or a fear of total loss goes farthest to weaken or unnerve the owner. In proportion as this loss or fear of loss is reduced, just so far is the public insurable interest diminished. A fear or a loss so small as neither seriously to unnerve nor to disable the owner is beyond the sphere of public insurable interest. For at that point where a man's disadvantage of fate comes within his reasonable ability to bear, the public welfare demands that the individual shoulder his loss himself. It is one of those hardships endurance of which makes for self-reliant citizenship.

Fire insurance now has no guide, no basic law by which to grant always an insurance ample enough to guard the public against the individual becoming a weakened member of the community; and also reciprocally to require of the individual that he carry an uninsured and inevitable share of the risk large enough to be

[1] "But the insured have it in their power to reduce fire losses to a very great extent. . . . . And they also have it in their power to also keep down the expenses."—Commissioner Cutting, Massachusetts, 1906.

[2] "In the practical operations of business it has become practically compulsory and property is now almost universally insured against loss by fire."—Wisconsin Joint Legislative Committee, 1913, p. 14.

wholesome and reasonably punitive against indifference toward our public fire waste.[1]

To attempt to fix an absolute distinction at this point may seem arbitrary and ill-adapted to men of various standards and qualifications. It is not, however, more arbitrary than the precedent which fixes twenty-one years as the age at which a man may vote, however superior or inferior to the normal he may be. The rule for the average person must be the community rule, the more especially because fire waste is increasingly regarded as a tax requiring a uniform rule of apportionment.[2]

Experience shows that property-owners rarely carry insurance in full. They are possessed of money or other property upon which they can rely in the event of total loss, and they deliberately assume some risk rather than bear the burden of larger premiums. From 60 to 90 per cent of their burnable wealth is the amount of insurance carried by the majority of men. Inquiry among credit and mortgage men indicates that they do not require merchants and builders to carry as much as 90 per cent unless the general credit of the insurer is low. In other words, the common experience shows that 90 per cent of insurance to value is ample and even exceeds ordinary needs. Such insurance, however, as now issued is valid from the bottom up; that is, the owner can begin to collect insurance from the first dollar of loss up to the full amount of his loss so far as it is covered by insurance. It is only when the loss exceeds the amount of insurance that the owner assumes any share of the burden.

If now we make our practice accord with what experience has taught us, we may assume that 90 per cent, but no more, of the burnable value is properly insurable in order to protect through the owner the public insurable interest. After thus filling out the public insurable interest, no moral ground remains on which further to ratify any form of wager contract and we are confronted by the principle that a principal should be not wholly relieved from penalty for neglect by himself or servants, hence, under the

[1] "Yet the security offered by fire insurance is undoubtedly one of the greatest causes of indifference to the cause of fire prevention."—Wisconsin Legislative Commission Report, 1913.

[2] "The fire loss is a direct tax on every industry, on every piece of property, and, indirectly, on every individual."—Commissioner Hartigan, Minnesota, 1910.

experience cited above, the remaining 10 per cent of burden must rightly be placed to the responsibility of the owner.[1]

This can be done only by providing that the owner shall not be able to collect any portion of any insurance until at least a loss of 10 per cent of the full burnable value has been incurred and that that much he must lose out of his own resources.[2] No one need purchase the full allowable or 90 per cent amount of insurance; he may purchase as much less as he wishes, but in that case he deliberately assumes the extra or voluntary plus the compulsory shortage and all shortage is charged to him in full on any loss before he can begin to collect.

To state the principle in the form of a working rule we may say: "All insurance shall be optional as to amount, not exceeding 90 per cent of burnable values, and shall invariably apply from the full value downward."

Such a law would develop a far fuller and more accurate accountancy of taxable values, besides forcing upon the owner his duty of stewardship through priority of risk.[3] It thus would recognize the great factor of public insurable interest, for buyers and sellers alike would be compelled to act in conformity with the public interest. This is not to say that "exemption," "average," "contribution," etc., have not long been limited features of certain insurance contracts, but all such will be found to fail to hold a public policy relation to the burnable value or true public risk.

Law in behoof of the public insurable interest would affect to the benefit of society every class of insured. The legitimate insured would profit directly himself; the careless man, the display

[1] "Fires are prevented by care. This care is merely good housekeeping. Except in a conflagration, construction has little to do with it, and even the faults of poor construction can be largely overcome by the care incident to good housekeeping and keeping property in good condition."—Commissioner Ekern, Wisconsin, 1914.

[2] "By far the greater number of fires are due to carelessness in some form. . . . . The fire companies can never be expected to bring about better conditions. A reasonable loss does not frighten them for they are only distributors and do not have the same interest in reducing the fire waste that the property owners have."—Commissioner Blake, Missouri, 1912.

[3] "It is only by radical legislation and by the strictest observance of our laws and by carefulness on the part of our people in their everyday life that we can ever hope to eliminate the needless fire waste of the country."—Commissioner Winship, Michigan, 1913.

merchant, the man who overclaims, and the incendiary—four classes in the community that either heedlessly or wantonly put unfair burdens upon the insurance funds—would be coerced into action that would mean greater regard for the rights of others.

The careless man has no working account of his burnable values; he fails to keep track of his insurance; he is negligent of all fire precautions.[1] In a word he transfers to the public the risk and burden of consequences in case of fire. This is the man who has frequent fires for which the community must pay. Suppose that such a man has an insurable property stated by him as worth ten thousand dollars and he takes out nine thousand insurance or 90 per cent, also assume that the policy form is worded to comply with the public insurable interest. In case of fire, if the loss be 10 per cent or over, then he definitely loses a thousand dollars, a strain perhaps sufficiently severe to cause him to repent of his careless habits and mend his ways.[2] Any loss over a thousand dollars he can collect up to the 90 per cent or $9,000 and he would not be overmuch hurt. If, after the fire, it was found that the burnable value was in reality $12,000, then under "public interest insurance" his $9,000 policy would insure him for but 75 per cent of the $12,000; he could not collect for loss under $3,000 and only for his loss in excess of that amount. His failure to keep track of his values as excuse for failure to pay his pro rata of the firewaste tax[3] with his fellow-citizens would automatically deduct from his power of recovery. If an owner deem these conditions a hardship and allege fear of repeated fires not incurred through neglect, then he is not entitled to insure on a normal basis and the needed relief also is in his hands; he can physically divide the property or not hold all the ownership precisely as is very usual for extra hazardous property.

[1] "Students of the subject all agree that the greater part of fires are easily preventable."—Wisconsin Legislative Commission, 1913.

[2] "Some means of bringing home to our citizens the true significance of this drain upon our comparatively small and poor state must eventually be discovered."—Commissioner Merrill, New Hampshire, 1913.

[3] "The point for us to bear in mind is that there will not be any reduction of the fire rate until the fire waste has been reduced."

"The people must be made to see that the remedy is within themselves, and when they fully realize this we can look for and will have results of a satisfactory nature."—Commissioner Harvey, Maine, 1912.

"Public interest insurance" might or might not suit the merchant who wishes to display an enormous area of goods. There are advantages to be gained in competition by exposing without obstruction a great mass of goods. Public-interest insurance, if applied to these great values, would make it impossible to dump the whole of this abnormal risk upon the public. Unless physically subdivided a million-dollar stock subject to one fire would stand to lose its owners all of the first one hundred thousand dollars. But if the goods were divided into four sections, the whole million of value would not be compelled to carry a greater initial liability than 10 per cent of $250,000, or $25,000. Surely these owners or trustees would not be harshly treated if society accept their plea of need to create such a risk up to 90 per cent and also require them to stand hostage for themselves and servants on 10 per cent.

Overclaims are most numerous on small losses. In cities the fires quickly put out, and so involving only a trifling loss, represent numerically over four-fifths of the total claims, and the insurance paid is in excess of the true loss in many of the cases because there is no practical way of proving the exorbitance of the claim. "Percentage collectors" manufacture thousands of such claims in spite of fire marshals,[1] the law, and the police. But with public-interest insurance placing a 10 per cent initial liability on the owner, a 1 per cent loss could not be put at 2 or 3 per cent, but would have to be sworn in at 11 per cent to recover the 1 per cent. Similarly a 5 per cent loss would have to be sworn in at 15 per cent to attempt to collect the 5 per cent. This would be far more difficult and dangerous than overclaims now are and could seldom succeed.

The incendiary is the most direct offender in making wrongful gains at public expense through insurance.[2] A favorite method of his is to go to various insurance offices, concealing from each the fact that he is insured elsewhere and so securing policies for a multiple of the value of his property. Or he may insure at the

[1] "Some states have fire marshal departments which are more of a menace than a benefit."—Commissioner Barry, Michigan, 1909.

[2] "There are comparatively few cases where the owner or tenant voluntarily sets fire to his property."—Commissioner McCoy, Montana, 1912.

"The prosecution of cases of arson is a very important part of his work but it necessarily affects but a small part of the total number of fires."—Wisconsin, Joint Legislative Commission, 1913, p. 71, on state fire marshal.

true value and later secretly remove the best part of his goods, leaving enough to support his claim in case the property is not completely destroyed. If he should insure 100 per cent of goods at 400 per cent value and the fire should be so complete as to leave no evidence of his deceit and his statement of values thus become the only face evidence and leave no course open save to accept the statement as true, he would still find that he had assumed in fact an initial loss of 40 per cent of all the actual value. His collection would be short in any event, in or out of court.

The legitimate insured form the great majority of property-owners and they cannot *en masse* insure to advantage by any method counter to the broad interest of the public they so largely compose. Public-interest insurance would benefit this great typical body of the insured in many ways. A few of the more important advantages are listed below:

1. By insuring at 90 per cent and assuming the first 10 per cent of the risk, the insured could collect more in case of total loss than he can under his present practice of attempting to economize by saving 20 per cent or more at the top of his values.

2. He could more than afford to insure to the full 90 per cent because he would benefit from the reduction in the cost of insurance that would immediately be due (especially in cities) on his assuming for himself all small losses and not imposing on the public the utterly disproportionate expense and overclaims attending minor claims. Few people realize how large such saving would be or how easily the same can be determined.

3. He could look for a second large saving in the reduction of the fire cost chargeable to careless neighbors. The careless ones might not become immediately heedful, they might continue to expect fires and to put their main reliance on the fire department's services, but the wholesome initial burden which the careless owners would be obliged to bear would be a direct reduction of public insurance costs. There is possibility for immense improvement here, as all authorities agree that most fires are due to careless indifference.[1]

[1] "The chief factor responsible for this situation is general carelessness and the utter lack of personal responsibility for the removal of causes productive of fires."—Excerpt from resolution passed at National Convention of State Fire Commissioners at Milwaukee, August, 1911.

4. The legitimate insured could expect from public-interest insurance an additional saving through decrease in incendiarism.

5. The fact that no "blanketing" or dividing of insurance policies could evade public-interest insurance would develop a fifth source of saving. The only possible method of reducing the owner's liability would be to divide the burnable values. This would be an incentive toward the more general use of separated and subdivided buildings which by limiting spread of fire also lessen the need for huge fire departments.

6. As every city fire is a potential conflagration,[1] the broad interests of city and country would be safeguarded in proportion as the frequency of city fires became lessened.[2]

Public-interest insurance addresses itself to the economic and moral problem that arises out of the "general carelessness and the utter lack of personal responsibility" testified to by state reports. Fire waste is being studied on many sides and a campaign of education is urged by public men. Meanwhile, the faulty organic law under which our insurance business is conducted tends to educate our citizens to divest themselves of all personal responsibility. In this dual system of education our jurisprudence seems to have control, as is evidenced by the increasing abnormality of our fire waste and by the increasing frequency of fires. Without a sound law to recognize the public insurable interest it is but natural that world-wide insurance should be a mere medley of contracts of grace regulated by commercial conditions. This state of affairs is not limited to separate localities, and has already had its public concern remarked on by the United States Supreme Court.[3]

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[1] "In the large cities there is a conflagration hazard. A fire may start in New York today which may make such calculations ridiculous and bankrupt most of the companies of the world."—New York Joint Legislative Commission, 1911.

[2] United States Geological Survey, *Bulletin 418*, "The Fire Tax and Waste of Structural Materials in the United States," by Wilson and Cochrane, 1910, says: "The danger of conflagration is present in every city and village in the United States, and with it the possibility of large loss of life."

[3] "We have shown that the business of insurance has very definite characteristics, with a reach of influence and consequence beyond and different from that of the ordinary businesses of the commercial world, to pursue which a greater liberty may be asserted."—*German Alliance Insurance Co.* v. *Kansas*, 233 U.S. 389.